UNITED STATES BANKRUPTCY COURT
DISTRICT OF MASSACHUSETTS
EASTERN DIVISION

In re: 655 CORPORATION, Debtor.	Chapter 11 Case No. 06-13020 (JNF)

OPPOSITION OF CATHAY BANK TO DEBTOR'S MOTION FOR AN ORDER (A) AUTHORIZING POSTPETITION FINANCING ON A PRIORITY SECURED BASIS; (B) SCHEDULING FINAL HEARING ON FINANCING; AND (C) GRANTING RELATED RELIEF

Cathay Bank ("Cathay"), as successor to General Bank, a secured claimant in this matter, hereby opposes the *Motion For an Order (A) Authorizing Postpetition Financing on a Priority Secured Basis; (B) Scheduling Final Hearing on Financing; and (C) Granting Related Relief* (the "Motion") filed by 655 Corporation (the "Debtor"). As is set forth more fully below, while Cathay does not object to the general terms of the proposed financing set forth in the Motion for the stated purpose of completing construction of the Debtor's real estate project and selling the units in order to preserve and enhance the value of the Debtor's asset, Cathay does object to the Motion in that it fails to make adequate provisions for the payments required under 11 U.S.C. § 362(d)(3) in cases, such as this one, involving single asset real estate debtors and otherwise to provide sufficient adequate protection of Cathay's interest in the Debtor's property. In addition, there is information lacking in the Motion that is necessary to assess whether the Debtor has met its burden under § 364 of the Bankruptcy Code. Accordingly, any approval of the post-petition financing sought in the Motion should be conditioned upon the Debtor's remedying the deficiencies set forth herein. In further support of this opposition, Cathay states the following.

Background

1. 655 Corporation, a Massachusetts corporation, filed a voluntary petition under Chapter 11 of the United States Bankruptcy Code on or about September 1, 2006 (the "Petition Date"). The Debtor continues to manage its property as a debtor-in-possession under §§ 1107 and 1108 of the Bankruptcy Code.

2. The Debtor is the owner of a single building that includes approximately eighteen (18) residential condominium units in various stages of completion and fifty-two (52) parking spaces located at 653-659 East 2nd Street, South Boston, Massachusetts (the "Property" or the "Project").

3. The Debtor in this case qualifies as a "single asset real estate" debtor as that term is defined in 11 U.S.C. § 101(51B), in that it is the "owner of real estate property or project (other than residential real property with fewer than 4 residential units) that generates substantially all of the debtor's income and on which the only substantial business being conducted by the debtor is that of operating the real property and activities incidental."

4. Cathay holds a claim secured by a mortgage on title to the Property. The claim arises out of a construction loan in the original principal amount of $5,600,000 by Cathay's predecessor in interest, General Bank (the "Loan"). The closing relating to the loan occurred on or about May 14, 2003 (the "Closing Date"). As of the Petition Date, Cathay's claim was in the approximate amount of $6,033,731.68.[1]

[1] This amount consists of principal and interest through September 1, 2006, but expenses through only June 30, 2006.

5. As of the Closing Date, the mortgage securing the Loan was believed to be a first mortgage. In fact, a mortgagee's title insurance policy issued to Cathay indicates that Cathay does indeed hold a first mortgage. An action filed in the Massachusetts Land Court in which New England Phoenix Co., Inc. ("NEPCO") asserts that the mortgage it held on title to the Property was fraudulently discharged, and in which a lis pendens has issued, has called that belief into question, raising the possibility that there is an encumbrance of up to $700,000 that has priority over Cathay's mortgage.

6. The Debtor states that the Project is approximately seventy-five percent (75%) complete. The Motion, however, does not provide specific information as to what work remains to be done over the designated four-month period of construction, other than noting that the model unit and remaining units require completion. Motion at ¶ 4.

7. Through the Motion, the Debtor has sought authority to obtain debtor-in-possession financing from another of its pre-petition lenders, LBM Financial, LLC ("LBM") in the aggregate amount of $2,000,000 (the "DIP Financing"). The DIP Financing would have an applicable fixed interest rate of fifteen percent (15%) per annum that is payable monthly from an interest reserve. In addition, the obligations arising as a result of the Debtor's receipt of this funding will be secured by a mortgage on the Property that is junior to liens held by Cathay, as well as to the Massachusetts Land Court litigation plaintiff to the extent it is ultimately determined to hold a secured claim that holds priority, and a professional fee carve out of "fees allowed by the Bankruptcy Court which are in excess of retainers and senior to all other liens and security interests" with respect to the Property. Motion at ¶ 10. However, the Debtor proposes that the mortgage on the Property securing the DIP Financing be senior to the lien held by

National Lumber Company and the pre-petition liens held by LBM, the proposed DIP Financing lender.

8. The Debtor claims that the financing sought to be advanced by LBM is in the amount necessary to "pay overhead costs, operating expenses, loan servicing costs, administrative and professional fees, and construction costs". Motion at ¶ 9. More specifically, the Debtor states that the DIP Financing will be used to fund (1) a post-petition retainer for Debtor's counsel in the amount of $70,000; (2) a four-month construction budget in the aggregate amount of $1,302,369; (3) an interest reserve for Cathay in the amount of $234,000; and (4) an interest reserve for LBM in the amount of $120,500. The remaining funds will be used for overhead, general and administrative, and other loan costs over a twelve-month period. Motion at ¶ 8.

9. While Cathay does not object to the purpose of the financing or the granting of a lien on the Property to secure the Debtor's resulting obligation that is subordinate to Cathay's lien, Cathay does object to the Motion's failure to afford sufficient adequate protection of Cathay's interests in the Property.

Argument

10. "As a general principle the Bankruptcy Code recognizes the primacy of pre-petition contractual liens and seeks to preserve financial interests created thereby." *In re Mosello*, 195 B.R. 277, 287 (Bankr. S.D.N.Y. 1996). Section 364(d) of the Bankruptcy Code provides the following:

> (d)(1) The court, after notice and a hearing, may authorize the obtaining of credit or the incurring of debt secured by a senior or equal lien on property of the estate that is subject to a lien only if—
>
> (A) the trustee is unable to obtain such credit otherwise; and

> (B) there is adequate protection of the interest of the holder of the lien on the property of the estate on which such senior or equal lien is proposed to be granted.

11 U.S.C. § 364(d).

11. The Debtor bears the burden of demonstrating both requirements under § 364(d). *See, e.g., In re Shaw Indus., Inc.*, 300 B.R. 861, 865 (Bankr. W.D. Pa. 2003); *In re Seth Co.*, 281 B.R. 150, 153 (Bankr. D. Conn. 2002); *In re Mosello*, 195 B.R. at 287; *In re Tenney Village Co., Inc.*, 104 B.R. 562, 564 (Bankr. D.N.H. 1989).

12. Generally, the Debtor's obligation to demonstrate adequate protection is to insure that the creditor receives the value for which it bargained. *Shaw Indus.*, 300 B.R. at 866; Mosello, 195 B.R. at 288; *In re Swedeland Dev. Group, Inc.*, 16 F.3d 552, 564 (3d Cir. 1994; H.R. Rep. No. 595, 95th Cong., 1st Sess. 339 (1977), reprinted in 1978 U.S. Code Cong. & Admin. News, pp. 5787, 6295. The goal of adequate protection is to "safeguard the secured creditor from diminution in the value of its interest during the Chapter 11 reorganization." *Mosello*, 195 B.R. at 288, *quoting In re 495 North Central Park Ave. Corp.*, 136 B.R. 626, 631 (Bankr. S.D.N.Y. 1992).

13. While Cathay recognizes that the retention of its priority and at least the first few budgeted interest payments both are important steps toward the Debtor adequately protecting Cathay's interest, those actions are not sufficient to effectively protect Cathay against diminution in its collateral value. In order to protect Cathay's interest, it is imperative that the Debtor provide additional information not adequately delineated in the Motion.

14. The Debtor proffers that Cathay's interest is adequately protected because, in part, the Property's value will be enhanced through the DIP Financing in that

completion of the units will facilitate their sale. However, courts have rejected "the notion that development property is increased in value simply because a debtor may continue with construction which might or might not prove profitable". *Swedeland Dev. Group, Inc.*, 16 F.3d 552, 566. To assure that the on-going construction is actually enhancing the value of Cathay's construction, or at least not diminishing it, Cathay should be afforded additional information provided on an on-going basis regarding the construction and sale process.

15. Therefore, in consideration of and as adequate protection, the Debtor should provide Cathay with a copy of the contract with the Debtor's chosen contractor, Lacourse Construction. Cathay should also receive and be afforded the opportunity to review the construction budget, requisitions or other requests for payment submitted by the contractor, other project allowances, finish schedules, evidence of payment of the invoices in the form of copies of cancelled checks or wire transfer confirmations, and any other documents related to the construction agreement and budget. In addition, once construction is completed or near completion and the sale process is undertaken, Cathay should also be provided copies of any listing agreements or other agreements with brokers, sales agents or others engaged for the purpose of offering the debtor's assets for sale, as well as any offering or marketing materials prepared by any such brokers or agents or otherwise used by the debtor in its marketing efforts.

16. Additionally, Cathay should have the right, upon reasonable notice to the Debtor and without the necessity of seeking this Court's authority under Rule 2004 of the Federal Rules of Bankruptcy Procedure, to inspect the Project, and to review the books and records of the Debtor relating to the on-going construction.

17. Adequate protection considerations also mandate that arguably ambiguous representations in the Motion as to the lien priority being granted LBM be clarified. In most references it is clear that Cathay's lien will retain priority over the lien being granted to LBM. There is a reference in the bullet points of the Loan Commitment attached to the Motion as Exhibit A, however, that indicates that "Security for the DIP Loan will consist of a first priority mortgage on the Real Estate junior to the existing first lien of Cathay." The internally inconsistent reference to a "first priority lien" that is "junior" must be clarified in order to properly reflect the lien priority uniformly recited in other parts of the Motion.

18. Additionally, there are certain additional budget provisions that, while not necessarily improper, are difficult to interpret or may be inadequate. For example, it is unclear why a single-asset real estate debtor that is engaging in construction through a general contractor and later offering units for sale through a broker would need to support a payroll of between $5,000 and $6,250 per month. While Cathay's presumably superior lien right affords a certain degree of irrelevance to the amount of the debt being incurred by the Debtor to LBM, in the event the Debtor's projections prove optimistic and Cathay is left to share with undersecured creditors in receiving distribution from the proceeds of whatever unsecured assets may exist, the amount of other debt sharing from that same pool will include LBM and, therefore, the amount of its claim will spring into relevance. Therefore, the Debtor should provide information as to who is being paid, what services he, she or they are performing and the benefit those services are affording to the estate.

19. Perhaps most importantly, the budget of approved expenditures in the DIP Financing fails to make adequate provisions to comply with § 362(d)(3)'s mandates

relating to single asset real estate cases, creating a substantial risk that, the Debtor's efforts notwithstanding, Cathay and perhaps NEPCO will have a right to relief from stay before marketing and sales efforts are completed.

20. Section 362(d)(3) provides that a single asset real estate debtor must, within ninety days of a case's commencement, either file a confirmable plan or make monthly payments to a secured claimant equal to the amount of interest accrued at the non-default contract rate on the value of the creditor's interest in the property. 11 U.S.C. §362(d)(3). The failure of a debtor to meet one of those two requirements entitles a secured claimant to relief from stay.

21. The Debtor commenced this case on September 1, 2006. The 90th day will pass on or about November 30, 2006, or less than thirty days from the filing of this Opposition.

22. The budget attached to the Motion provides for interest payments to Cathay of $46,000, which does approximate the contract rate of interest accrued on Cathay's claim, in the months of October through December. The interest payments to Cathay, however, taper off starting in January and continuing downward thereafter, presumably based on some assumed unit sale projection. In the event the unstated sales projections prove optimistic, the Debtor will be in violation of § 362(d)(3)'s provisions in or around January, 2007.

23. At minimum, the entry of any order should not be deemed a determination that the payments set forth in the budget constitute adequate protection of Cathay's interest in the Debtor's property, that Cathay has waived any rights or remedies to which it may be entitled for any reason, including, but not limited to, that the payments

envisioned in the budget fail to afford Cathay adequate protection or that the order approving the budget estops Cathay from being granted relief from stay due to the Debtor's failure to comply with § 363(d)(3).

24. The better cure for the problem, however, is that the budget should be modified to enable the Debtor to make all interest payments to Cathay assuming no sales occur or that the sales do not occur as quickly as projected. While the $13,000 interest contingency for slow sales for the entire budget period provides a modicum of protection, the amount would, most certainly, not be sufficient if the units were not sold as projected.

25. On a related note, the potential payments to which NEPCO might be entitled under § 363(d)(3) are not budgeted, which is problematic if its mortgage is reinstated. This does interpose an adequate protection issue for Cathay as the prospect of a previously unknown but potentially higher priority lien creditor being entitled to relief from stay, as well as that creditor accruing unpaid interest, presents the risk of Cathay suffering a diminution in the value of its interest in the Debtor's property.

26. Even were the appropriate and mandatory payments properly budgeted, however, additional modifications would be required to ensure adequate protection of Cathay. The Motion and DIP Financing commitment both reflect that the Debtor cannot make any payments of over $3,000 without LBM's consent. However, as a practical and administrative implication, such a restriction would mean that LBM's consent would be required for payment of interest to Cathay, effectively giving a junior lender control over the Debtor's compliance with statutory payment obligations to Cathay. Accordingly, there should be either an exception to the consent provision for payments of Cathay

interest, or LBM should be deemed to have consented to the payments set forth in the budget.

27. Finally, the current construction budget of $1,302,369 has an included contingency amount of $20,000, which equals approximately 1.56%. This appears to be unrealistically low in relation to completing construction over a four-month period. At minimum, the difficulty in evaluating the sufficiency of the budgeted construction reserve underscores the paucity of information in the Motion relating to the tasks left to actually complete the Project.

WHEREFORE, Cathay respectfully requests that the Motion is denied unless the Debtor provides additional information regarding the terms of the budget and DIP Financing and adequately protects Cathay's interest as set forth herein.

Respectfully submitted,

CATHAY BANK

By its attorneys,

HOLLAND & KNIGHT, LLP

/s/ John J. Monaghan

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Dated: November 3, 2006

CERTIFICATE OF SERVICE

I, John J. Monaghan, counsel to Cathay Bank, do hereby certify that on this 3rd day of November, 2006, I served copies of the foregoing *Opposition to Debtor's Motion for an Order (A) Authorizing Postpetition Financing on a Priority Secured Basis; (B) Scheduling Final Hearing on Financing; and (C) Granting Related Relief* by first-class mail, postage pre-paid, upon the parties listed on the service list attached hereto, who were not served via ECF.

/s/ John J. Monaghan

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Service List
665 Corp
Ch. 11 Case No. 06-13020
(Cathay Bank)

Allstate Painting Co., Inc.
34 Day Street
Norwood, MA 02062

Boston Police
Detail Billing Unit
P.O. Box 191776
Boston, MA 02119

Boston Water & Sewer Commission
980 Harrison Avenue
Boston, MA 02119

Buonasaro Construction
Peter Buonasaro
1408 Providence Highway
Norwood, MA 02062

C & C Tiling
55 Minot Street, Apt. 1
Boston, MA 02124

Colony Hardware Supply
1188 Dorchester Avenue
Boston, MA 02125

Curragh Construction
94 St. Marks Road
Boston, MA 02124

Door Systems, Inc.
120 Alexander Street
P.O. Box 511
Framingham, MA 01704

Extreme Plumbing
Ernie Cito
256 Washington Street
Boxford, MA 01921

Leamar Industries
171 Locke Drive
Marlborough, MA 01752

Lynco Fire Protection Inc.
19 Grant Avenue
Burlington, MA 01803

MA Waste Systems, LLC
300 Centre Street
Holbrook, MA 02343

Marr Scaffolding
One D Street
Boston, MA 02127

National Lumber
Rocky Carlino
71 Maple Street
P.O. Box 9032
Mansfield, MA 02048

R & R Sales, Inc.
174 Hampton Street
Boston, MA 02119

Richie's Insulation, Inc.
111 Old Bedford Road
Westport, MA 02790

Sani-kan Portable Sanitation
P.O. Box 16400
Rumford, RI 02916

Tristate Stone, Inc.
120 Southbridge Road
P.O. Box 762
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Tudor Plastering
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